Beware of Post Separation Debts in Divorce

By Mitchell A. Jacobs

Given the current state of the economy, it is not surprising that the debts incurred by spouses during marriage often become a hotly contested issue during a typical marital dissolution proceeding. Divorcing spouses are often shocked to discover the extent of credit card debt secretly incurred by their significant other during the marriage. With regard to less frivolous debt incurred during the marriage, such as hospital bills, the debt is typically allocated as part of the overall division of the community estate. However, complications arise when the debt is incurred after the parties separate. In such instances, various Family Code sections control and hold nondebtor spouses liable for certain "necessaries" incurred by the other spouse. Included among these necessaries are hospital and medical bills. However, what happens if the case proceeds to judgment, but the judgment does not assign this "necessary" debt to the nondebtor spouse? Is the nondebtor spouse still liable for the debt?

CMRE Financial Services Inc. v. Parton addresses these issues. In this case, the parties to the underlying marital dissolution action separated, and following the separation, the husband, Daniel, was admitted to Tri-City Hospital for severe emotional illness. By the time of his release from the hospital four days later, Daniel had incurred substantial hospital and medical fees. Thereafter, Daniel's wife Pamela filed a petition for dissolution of her marriage. In her financial disclosure documents, Pamela stated that Daniel's hospital debt belonged to Daniel. Subsequently, a judgment of dissolution was entered. The judgment did not assign Pamela any liability for Daniel's hospital and medical costs.

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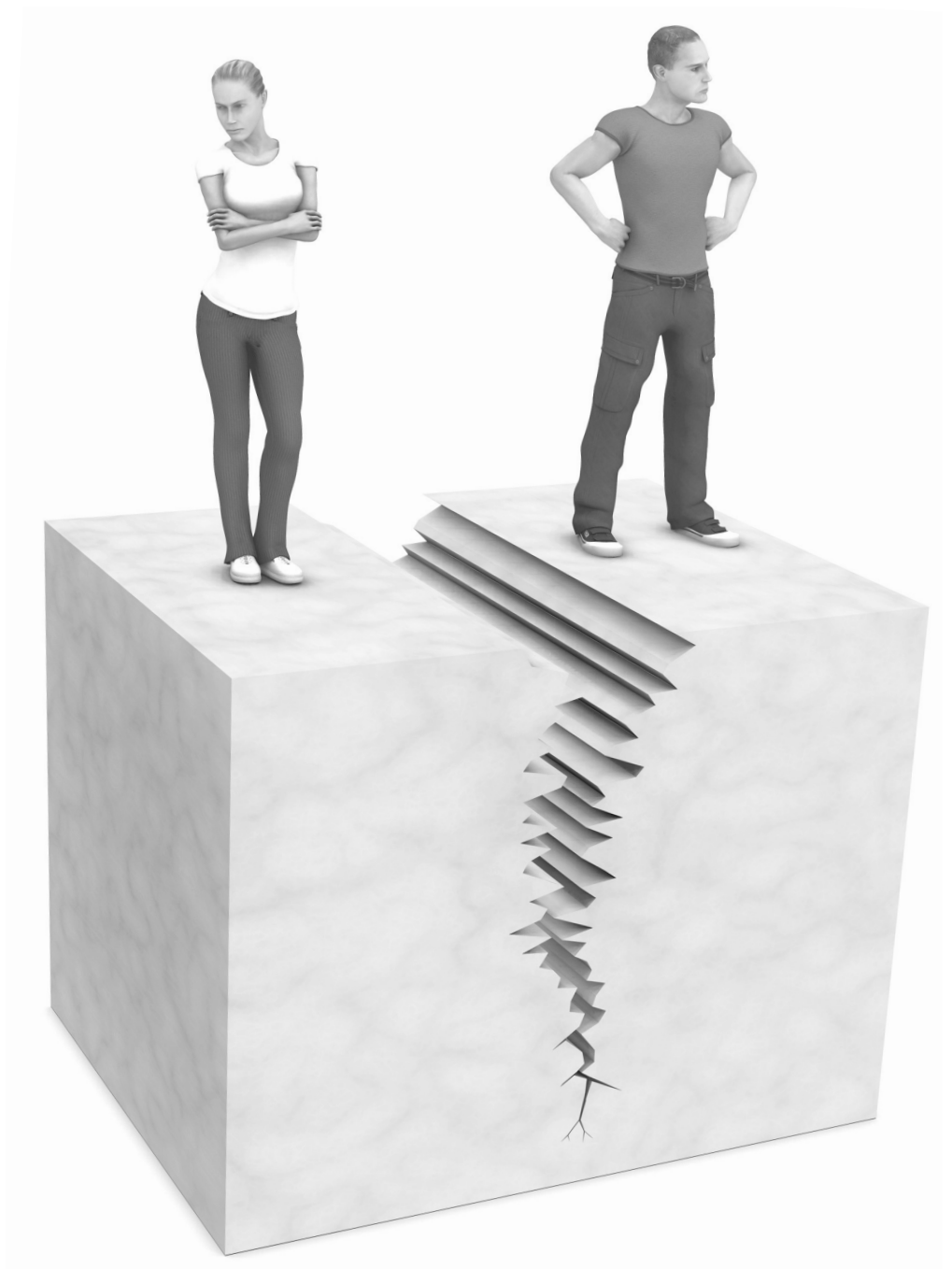
Thereafter, on Jan. 24, 2008, CMRE Financial Services, as assignee of Tri-City Hospital filed a complaint against Daniel and Pamela alleging that the parties owed $26,083, plus interest and attorney fees. Pamela filed an answer denying the material allegations of the complaint. Pamela also filed a cross-complaint alleging CMRE's violation of the Fair Debt Collection Practices Act. CMRE was unable to serve Daniel and he was dismissed from the action without prejudice. Thereafter, CMRE filed a demurrer alleging that Pamela was liable for Daniel's necessaries pursuant to the Family Code, and that Pamela was not relieved of that liability by virtue of her dissolution judgment. The trial court sustained CMRE's demurrer without leave to amend, and after a trial, entered judgment against Pamela for $26,083 plus interest, attorney fees and costs.

Pamela timely appealed. She argued that her dissolution judgment relieved her of any liability for her husband's debts. But where did Pamela's liability for Daniel's hospital bills arise from in the first place? After all, the parties were separated at the time Daniel was admitted to the hospital, why would Pamela be responsible for Daniel's post-separation medical bills? Family Code Section 914(a)(2) provides that a married person is personally liable for the debts incurred for common necessaries of life by the person's spouse while the spouses are living separately (except where there is a separation agreement between the spouses, the terms of the agreement will control). This was the basis for holding Pamela liable for Daniel's post-separation medical debt. However, rather than focus on the language of Section 914, Pamela argued that under Family Code Section 916(a)(2), she was not personally liable for the debt because the debt was not assigned to her for payment pursuant to the terms of the parties' judgment.

Specifically, Section 916(a)(2) provides that "notwithstanding any other provision of this chapter, the separate property owned by a married person at the time of the division and the property received by the person in the division is not liable for a debt incurred by the person's spouse before or during marriage, and the person is not personally liable for the debt, unless the debt was assigned for payment by the person in the division of the property." Here, Pamela argued that the judgment did not assign her Daniel's medical debt, thus she was not liable for the debt.

The appellate court agreed with Pamela and reversed the lower court's ruling. The court concluded that although Section 914 gave rise to Pamela's liability for the costs incurred by Daniel's necessaries, that liability was subject to the provisions of Section 916. Under Section 916, following dissolution of a marriage, a nondebtor spouse is only liable for debts incurred by the former spouse during their marriage if the debt is assigned to the nondebtor spouse by the judgment of dissolution. Since there was no such assignment, Pamela was not liable for Daniel's hospital debts.

Thus, it is clear that the terms of a dissolution judgment can act as a shield from civil creditors intent on recovering monies owed. Family law practitioners should be very clear that the debt at issue should be specifically assigned in the judgment. Failing that, *CMRE* makes it clear that relying on the default provisions of Section 914 is insufficient should the parties marriage be dissolved. Recent case law makes it clear the nondebtor spouse is only liable for the hospital debt if the debt is assigned to the nondebtor spouse pursuant to the terms of the judgment. Thus, if it is the intent of the parties to assign the debt to the nondebtor spouse, the assignment must be clearly stated in the judgment.



Taxes & Privacy, OH MY!

By Robert W. Wood

In this Internet age of ubiquitous Facebook, Twitter, and more, surely some things are meant to be, well, private. How much you make and what tax deductions you claim are probably more sacrosanct than your sex life. And yet the Supreme Court has recently decided not to review a case dramatically impacting taxpayers and privacy rights.

The decision is *United States v. Textron*, 577 F.3d 21 (1st Cir. 2009), cert. denied May 24, 2010. There's no dispute that if you are a U.S. citizen or permanent resident you must disclose and pay tax on your worldwide income. But what your advisors can be required to say — and precisely what backup documents you can be forced to disclose — are big-stakes questions.

Traditionally, all tax lawyers understood that documents to be used in the event of tax litigation (documents relating to the strength or weakness of a tax position) are covered by work-product privilege. They may be covered by attorney-client privilege too, but work-product privilege is important, a central precept of tax planning for generations. If you have attorney-client privilege, why do you care?

In the rough-and-tumble of business, many taxpayers show their tax memos and calculations to their accountants and consultants as well as their lawyers. That waives attorney-client privilege unless the taxpayer has ensured that the accountants and consultants are hired by the lawyers, not by the client directly. The idea of having the lawyer hire them is to import attorney-client privilege to all communications. It makes sense to do that if tax litigation is imminent or if you are hyper-sensitive to attorney-client privilege, as you might be with a potential criminal tax case. But it can be cumbersome otherwise, and most clients, especially businesses, don't want to go through this hassle.

Where there are large tax dollars at stake, the Internal Revenue Service pushes hard to get disclosure of any and all documents. That's what the *Textron* case was all about. Textron, a defense contractor, had many memos and calculations dealing with the likelihood of achieving particular tax results on audit of its complex tax positions.

The IRS pushed hard for disclosure, but Textron refused and went to court. Textron argued it was well-settled that the work-product doctrine protected these items. The federal district court agreed.

Aggressive and undaunted, the IRS appealed to the 1st Circuit Court of Appeals. The 1st Circuit affirmed the district court, upholding the work-product privilege. After all, these documents were about exactly what ended up happening — the IRS attacking tax positions and arguing for more tax. That made them well within established work-product purviews.

But the IRS then asked for *en banc* review of the case. The 1st Circuit granted *en banc* review and then reversed itself! Declining to shield the documents from the IRS, the 1st Circuit found that they were not prepared *specifically* for use in litigation. That meant they were not protected. In a ruling laced with strong policy overtones, the 1st Circuit admonished that collecting taxes was in the national interest and was no game.

Tax lawyers can justifiably be called myopic. Yet it is not hyperbole to say that *Textron* was a huge victory for the IRS, even bordering on frightening. Moreover, the fact that the Supreme Court has declined to review the case means the IRS view prevails. Technically, the case is binding only in the 1st Circuit. Yet many tax practitioners expect the IRS to assert *Textron* nationally. That means more care, at least in tax cases, is required.

Beyond tax matters, does *Textron* signal a general weakening of the work-product doctrine? The answer is almost certainly yes, and that is unfortunate. The new standard enunciated in *Textron* seems to focus on the degree of specificity with which something sought to be protected under the work-product doctrine is prepared. It is no longer enough for a document to be prepared in anticipation of litigation.

Now it seems, it must be explicitly "prepared for" litigation and specifically "for use" in litigation. These seemingly simple words and subtle nuances may yield decidedly non-subtle differences in result. In the past, work-product protection was generally available when documents were prepared because of the possibility of litigation, even though there may have been other purposes as well. As long as the document would not have been prepared no matter what, it was probably protected.

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Now, *Textron* says work papers must be "prepared for" — not "because of" — litigation. And a specific litigating intent seems required. Like Robert Frost's two diverging roads in the woods, this may make all the difference.

What lawyers and clients can do about this isn't clear. It may help if all of your notes and documents are prominently legended at the time they are created with "work-product" protections. It may also help if you are able to show that you are preparing these documents for the *specific* use of anticipated litigation. Such steps may be self-serving, but they are not vacuous.

Even better would be more rigorous attention to attorney-client privilege. Indeed, in the tax world, *Textron* will lead to more accountants being hired and supervised by tax lawyers. Attorney-client privilege, after all, still seems alive and well. Be careful out there.

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